



## **CIO OFFICE MORNING MARKET WRAP – Sunday September 12<sup>th</sup>, 2021. ALSO AVAILABLE ON ALEXA**

Last week was not good for global markets. Out of the 10 major asset classes which are part of our allocation framework, 9 were in the red and the one which wasn't, the high yield segment of fixed income, was up by an unimpressive 0.01%.

Cyclical assets, i.e., equities and listed real estate, took the largest hit: the recent downshift in growth momentum, linked to the relentless Delta variant, meets historically elevated valuations. This situation is certainly not new, but as the back-to-school season is on, several influential Wall Street strategists have done their homework and highlighted the risk of a near term correction - as well as modest expectable returns ahead. Peak growth and peak valuations are not a great combination, and market participants responded with a dip in sentiment. Headlines mention the worst weekly return since June, which is true, however global stocks actually lost slightly more than a percentage point in developed markets and less in their emerging peers. It's not even a consolidation.

Defensive assets however didn't benefit from this "risk-off" shift. Indeed, they have their own issues: inflation keeps on rising, as illustrated by latest PPI numbers, and more importantly, central banks in developed economies are about to start reducing their balance sheet-based support. The current economic situation doesn't justify the extraordinary stimulus measures in place anymore as, after all, global GDP is now only 2% below the pre pandemic level. The ECB last week illustrated the trend, with the announcement of a "moderately lower" purchase pace ahead. The RBA also followed through with their plans to scale back their QE. More inflation, and less liquidity: no surprise that interest rates were on the rise over the week, with the US 10-year Treasury yield closing at 1.34%.

We have been writing for some time about the combination of a softer macro episode with elevated valuations and the imminent start of tapering, which is why we expect some volatility. There is nothing new here. What matters is obviously what lies ahead, and we see reasons to remain on our reasonably constructive scenario. First, this Delta wave has started to fade, and vaccines have been fortunately quite effective in limiting hospitalizations and deaths. The pace of vaccinations is accelerating where it needs to, especially in Asia. To stay there, China last week saw two good news: better than expected trade numbers, and a high-level dialogue between Xi and Biden. Our sentiment is that we may have seen the peak in the momentum of growth, but we remain confident on the direction of travel as we may also be close to the trough of the current Delta-driven softness. By the way, all cyclical markets are not worried: oil prices remain steady, gaining 2% last Friday to end the week on a positive note, at \$73 for the Brent. Our regional stock markets continue to shine, with a positive 1% return last week for the MSCI GCC, lifting its year-to-date performance to 30%. They are an exception within emerging market stocks, but with fundamental reasons: the reopening of their economies combines with accessible valuations. Bottom-line, our monthly tactical asset allocation meeting held last week didn't change our current positioning. We overweight stocks and underweight bonds in a clear but carefully calibrated way, expressing our reasonably constructive view for the medium term, as well as our expectations for short-term volatility. Should risk-assets brutally go south on an episode of anxiety, we would certainly consider adding exposure.

The week ahead may actually fuel volatility, with potentially disturbing numbers on retail sales and inflation. We wouldn't be surprised to see some turbulences, and will also follow the electoral developments in Germany and Japan. Stay safe.

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